

# Memorandum

**To:** MARK LEJA,  
Construction Program Manager

**Date:** March 18, 2008

**Contract No.:** 08-334844  
**File No.:** P2200-0417A

**Attention:** MICHAEL KISSEL  
Chief, Office of Contract Administration

**From:** DEPARTMENT OF TRANSPORTATION  
Audits and Investigations

**Subject:** Special Audit Request – RMD Rebar Inc. Cost Escalation Claim

We completed a special request ~~audit of~~ costs claimed by RMD Rebar, Inc. (Contractor), a subcontractor to Washington Obayashi, Joint Venture (WOJV) under Contract No. 08-334844 between the Department of Transportation (Department) and WOJV. The Contractor has claimed costs of \$2,091,257.02 relating to labor and material escalation costs for the period of January 2007 through December 2007, in accordance with the Code of Federal Regulations (CFR) 48, Chapter 1, Part 31, the Department Standard Specifications and the Contract Special Provisions. The claimed costs are the responsibility of the Contractor's management and our responsibility, based on our audit, is to express an opinion on those claimed costs.

Our audit was conducted in accordance with the Performance Standards set forth in the *Government Auditing Standards* issued by the Comptroller General of the United States of America. These standards require that we plan and perform the audit to obtain reasonable assurance that the data and records reviewed are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and the records reviewed. It also includes assessing the accounting principles and significant estimates made by the Contractor's management, as well as evaluating the overall presentation. We believe that our audit provides a reasonable basis for our opinion.

The scope of the audit was limited to financial and compliance activities related to Contract No. 08-334844 and the allowability of the proposed claim in accordance with the requirements set forth by the Department Standard Specifications, Contract Special Provisions and CFR 48, Chapter 1, Part 31. The audit consisted of determining the reasonableness of the labor and materials escalation costs claimed for February 2007. Transactions arising subsequent to December 2007, were not tested and, accordingly, we do not express an opinion on costs or credits arising after this

date. Our audit included such tests as we considered necessary to achieve the following objective:

- To determine if the costs claimed are supported and reflect costs allowable under the CFR 48, Chapter 1, Part 31.
- To determine if the costs claimed are in compliance with the Department Standard Specifications.

## AUDIT RESULTS

In our opinion, the Contractor has not fully supported the costs claimed in the amount of \$2,091,257.02 related to escalation cost claims for labor and materials for the period of January 2007 through December 2007. Based on our audit of the Contractor's project cost records and interviews with the Contractor and Department construction personnel, we determined the Contractor can support \$1,671,438.42 (See Exhibit A). The following exceptions were noted:

### Finding 1

The Contractor has claimed \$244,505.04 in labor escalation costs for the period of January 2007 through December 2007. Based on our audit, we determined the Contractor can support labor escalation costs of \$113,711.27. Therefore, the claimed cost is overstated. FAR 31.201-3 – Determining Reasonableness states, in part:

*"A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business..."*

**Recommendation:** We recommend the Department disallow \$130,793.77 of the \$244,505.04 claimed for January 2007 to December 2007 labor escalation costs.

### Finding 2

The Contractor has claimed \$1,846,751.98 in material escalation costs for the period of January 2007 through December 2007. Based on our audit, we determined the Contractor can support material escalation costs of \$1,557,727.15. Therefore, the claimed cost is overstated. FAR 31.201-3 – Determining Reasonableness states, in part:

*"A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business..."*

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**Recommendation:** We recommend the Department disallow \$289,024.83 of the \$1,846,751.98 claimed for January 2007 to December 2007 material escalation costs.

The audit findings were discussed with ChiaChi Wang, District 8 Construction Engineer and Vern Jones, Construction Coordinator on February 26, 2008.

This report is intended for the information of the Department's management, the Federal Highway Administration, and the Contractor. However, this report is a matter of public record and its distribution is not limited.

If you have any questions concerning the audit, please contact Ryan Baer at (916) 323-7882.

**ORIGINAL SIGNED BY:**

RYAN BAER  
Auditor

Approved:

**ORIGINAL SIGNED BY:**

CARLOS M. AGUILA  
Audit Manager

Attachments

c: VJones, HQ Construction Coordinator  
CWang, District 8 Construction Engineer

**EXHIBIT A - SUMMARY OF FINDINGS**

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RMD Rebar, Inc.

**SUMMARY OF AMOUNTS AUDITED**

<b>Description</b>	<b>Cost Claimed</b>	<b>Supported Costs</b>	<b>Questioned Costs</b>	<b>Notes</b>
January 2007 - December 2007 Labor Escalation	\$ 244,505.04	\$ 113,711.27	\$ 130,793.77	See Exhibit B
January 2007 - December 2007 Materials Escalation	1,846,751.98	1,557,727.15	289,024.83	See Exhibit C
	<u>2,091,257.02</u>	<u>1,671,438.42</u>	<u>419,818.60</u>	

**EXHIBIT B - Labor Escalation****P2200-0417A****08-334844****RMD Rebar, Inc.**

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	<b>Claimed</b>	<b>Supported</b>	<b>Questioned</b>	<b>Notes</b>
RMD Rebar	\$ 221,733.96	\$ 104,485.45	\$ 117,248.51	<b>A,B</b>
Fontana Steel	22,771.08	9,225.82	13,545.26	<b>A,B</b>
	<u>244,505.04</u>	<u>113,711.27</u>	<u>130,793.77</u>	

**Notes**

**A** RMD Rebar has claimed escalation for the month of January 2007. Per CCO 317, the District has agreed to pay escalation as of February 1, 2007. Therefore, we have disallowed labor escalation cost claimed by RMD and Fontana Steel for January 2007:

RMD Rebar	\$ 18,502.89
Fontana Steel	10,739.01
	<u>29,241.90</u>

**B** To determine the reasonableness of the benchmark rate used to determine the escalation rate to be applied to supported hours, we established a weighted average rate for each of the above classifications using the prevailing wage rate determinations. The weighted rate was based on the relevant prevailing wages from March 2004 to January 2007 (35 months). We believe the weighted average calculated is a reasonable benchmark, as these rates are the actual rates required to be paid during the period of the contract. See page 2 of Exhibit B:

**EXHIBIT B - Labor Escalation**

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		RMD Rebar		
		Escalation Rate		Audits Weighted
Period	Position (1)	(2)		Average Rate (3)
1/1/07 to 3/31/07	Foreman	\$	6.99	\$ 3.58
1/1/07 to 3/31/07	Journeyman		6.79	3.26
4/1/07 to 6/30/07	Foreman		6.81	3.58
4/1/07 to 6/30/07	Journeyman		6.62	3.26
7/1/07 to 6/30/08	Foreman		9.74	5.90
7/1/07 to 6/30/08	Journeyman		9.42	5.27

- (1) Per union agreement. Foreman receive 10 percent salary increase over the established journeyman prevailing rate. We have calculated the 10 percent increase into our weighted rate analysis.
- (2) RMD Rebar has included a 16 percent surcharge and 28 percent mark-up to the escalation rate. CCO 317 only includes compensation for escalation costs incurred by the contractor. Therefore, we have not included the surcharge and mark-up in our weighted average rate.
- (3) The Weighted average rate was based on prevailing wage determinations for Iron workers. We weighted the rates based on the duration of time each prevailing wage rate was in effect during the contract. We then established a benchmark rate for the duration of the contract. We then took the difference between the benchmark rate and the prevailing wage rate applicable during the specified delay period to establish the labor escalation amount or "delta" to be paid per delay labor hour. Below is an example weighted rate calculation:

Period from 1/1/07 - 3/31/07				
Example: Iron Worker (Journeyman)				
PW Period	Rate PW	Months Ratio	Weighted Average	Delta
3/1/04 - 6/30/04	\$44.15	0.11	\$4.86	
7/1/04 - 6/30/05	\$45.92	0.34	\$15.61	
7/1/05 - 6/30/06	\$47.67	0.34	\$16.21	
7/1/06 - 6/30/07	\$49.92	0.20	\$9.98	
			<u>\$46.66</u>	
Escalation amount (\$49.92 - \$46.66)				\$3.26

**EXHIBIT C - Materials Escalation****P2200-0417A****08-334844****RMD Rebar, Inc.**

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	<b>Claimed</b>	<b>Supported</b>	<b>Questioned</b>	<b>Notes</b>
RMD Rebar	\$ 1,846,751.98	\$ 1,557,727.15	\$ 289,024.83	<b>C,D</b>

**Notes**

C Below is the materials escalation claimed from January 2007 to December 2007. The \$114,688.87 claimed by RMD for January 2007 was supported, however, CCO 317 only allows escalation cost from February 2007. Therefore, we have disallowed the claimed cost for January 2007.

<b>Month</b>	<b>Claimed</b>	<b>Questioned</b>	<b>Supported</b>
Jan-07	\$ 121,138.00	\$ 121,138.00	\$ -
Feb-07	227,619.00	-	227,619.00
Mar-07	136,871.87	-	136,871.87
Apr-07	266,700.05	-	266,700.05
May-07	289,052.84	-	289,052.84
Jun-07	204,269.39	-	204,269.39
Jul-07	97,750.45	-	97,750.45
Aug-07	116,097.71	-	116,097.71
Sep-07	63,171.41	-	63,171.41
Oct-07	84,539.09	-	84,539.09
Nov-07	62,317.21	-	62,317.21
Dec-07	9,338.13	-	9,338.13
	<u>1,678,865.15</u>	<u>121,138.00</u>	<u>1,557,727.15</u>

D Mark-ups apply for extra work at force account. CCO 317 allows only for escalation costs. Therefore, we have disallowed the claimed mark-ups.

	<b>Claimed</b>	<b>Questioned</b>	<b>Supported</b>
Mark-up	\$ 167,886.83	\$ 167,886.83	\$ -